

No. 11939

IN THE

United States Circuit Court of Appeals
FOR THE NINTH CIRCUIT

DIVISION OF LABOR LAW ENFORCEMENT, STATE OF
CALIFORNIA,

Appellant,

vs.

PAUL W. SAMPSELL, Trustee in Bankruptcy of the Estate
of C. A. Reed Furniture Company, Bankrupt,

Appellee.

APPELLANT'S OPENING BRIEF

PAULINE NIGHTINGALE, and
EDWARD M. BELASCO,

503 State Building, Los Angeles 12,
Attorneys for Appellant.

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Opinion Below

The court below did not file a written opinion. The order affirming the order of the referee in bankruptcy is set forth in the record at pages 39 to 41 inclusive.

Jurisdiction

This proceeding arose in the District Court of the United States for the Southern District of California, Central Division, when a petition in bankruptcy was filed. Following adjudication and general reference, Appellant, as statutory assignee of wage claimants who were former employees of the bankrupt, filed its Proof of Unsecured Debt in Bankruptcy (Priority) [R. 2-4], whereupon Appellee filed Notice of Hearing on Objections to Claim of G. O. Thrailkill [R. 42-43], Appellant's Los

Angeles office supervisor who signed the proof of debt above. On December 16, 1947 a hearing was held before the referee in bankruptcy, and the referee's Order Determining Extent of Priority of Employee's Claims [R. 4-5] was rendered on January 8, 1948. Appellant filed its Petition for Review of Referee's Order Determining Extent of Priority of Employees' Claims [R. 32-36] on January 29, 1948. The referee in bankruptcy on February 4, 1948 issued his Amendment to Order of January 8, 1948 [R. 30-31] and filed his Referee's Certificate on Review on February 5, 1948 [R. 37-39]. By Stipulation to Supplement Record [R. 6-30] filed on February 5, 1948 the collective bargaining agreements between the bankrupt and the unions to which Appellant's assignors belonged were made part of the record of the case. Following a hearing in the District Court, the district judge entered his Order Affirming Order of Referee [R. 39-41] on April 12, 1948, and Appellant filed its Notice of Appeal [R. 41-42] on May 3, 1948.

The jurisdiction of this Court to hear and determine this appeal is conferred by Sec. 24(a) of the Bankruptcy Act, as amended, and Sec. 128(c) of the Judicial Code.

Question Presented

If an employee's eligibility for vacation pay occurs during the three months' period prior to the commencement of the bankruptcy proceeding of his employer, is all of the unpaid vacation pay entitled to priority status as wages earned within the provisions of Sec. 64a(2) of the Bankruptcy Act?

Statute Involved

Sec. 64a of the Bankruptcy Act (U.S.C. Title 11, Ch. 7, Sec. 104) provides:

“The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment shall be (1) . . .; (2) wages, not to exceed \$600 to each claimant, which have been earned within three months before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) . . .”

Statement of the Case

The facts are not in dispute. Appellant's assignors, former employees of the bankrupt, were members of either the Upholsterers' Union, Local No. 15, or the Furniture Workers' Union, Local No. 3161. The collective bargaining agreements mentioned above were in full force and effect during all periods referred to herein. Although the entire agreements are set forth in the record, pages 7-30, for the Court's convenience the vacation clauses of the agreements are here set forth:

1. The vacation clause of the Upholsterers' Union collective bargaining agreement:

“VII.

“Vacation.

“The employer's established personnel covered by this Agreement who have been in the employ of the

Employer for one year, or more, and who have been in continuous good standing of the Union, shall receive a week's vacation with forty (40) hours' pay at the wage rate prevailing immediately prior to the vacation. Such vacation shall be taken at a time mutually agreeable to the employee and the Employer. Employees with five years' service shall receive two weeks' vacation with pay."

2. The vacation clause of the Furniture Workers' Union collective bargaining agreement (omitting portions concerning veterans which are not at issue):

"Article VII.

"(a) Each employee shall receive one (1) weeks vacation after one (1) year of service with the Company and two (2) weeks vacation after three (3) years of service with the Company, except that this liberalized vacation benefit shall not apply to those employees who have taken their 1946 vacations.

"(b) Vacations shall be taken during July, August, or September and vacation pay shall be computed at any time it accrues during that period.

"(c) . . . (veterans—omitted portion.)

"(d) Week's vacation as used herein is understood to be 40 hours times the straight time hourly rate at the time vacation is due.

"(e) In the event an employee has worked a full year for the Company and then terminates his employment, he shall be entitled to receive his earned vacation pay. There shall be no pro-rata vacation."

Bankruptcy of the employer ensued shortly after the employees completed their year's eligibility period to qualify for vacation for the vacation year 1946-47, and none received his vacation. The Appellee, trustee in bankruptcy, made an accurate breakdown of the payroll records of the bankrupt and correctly calculated all vacation pay earned by the employees. At the hearing before the referee in bankruptcy, Appellee contended, and this contention was sustained by the referee and the district judge, that only one-fourth of the vacation pay due was entitled to priority status under Sec. 64a(2) of the Bankruptcy Act, since one-fourth of the vacation pay represented vacation pay earned during the three months prior to bankruptcy, and that the remaining three-fourths of the vacation pay was entitled only to general claim status since it represented vacation pay earned more than three months prior to bankruptcy. Appellant's contention is that the condition precedent to the earning of vacation pay by an employee under either collective bargaining agreement is the completion of a designated period of continuous service with the employer, and since the designated period of service was completed by each employee herein during the three months prior to bankruptcy, the entire vacation pay was then and there earned and therefore was entitled to priority status under Sec. 64a(2) of the Bankruptcy Act. Following the adverse ruling on this point of law, the Notice of Appeal was filed.

Specification of Error

The District Court erred as follows:

1. The Court erred in rendering its Order of April 12, 1948 in which the Order of the Referee in Bankruptcy of January 8, 1948, as amended on February 4, 1948, was confirmed.

2. The Court erred in ruling as a matter of law that Appellant's assignors' vacation wages were not entitled to priority status under the provisions of Sec. 64a(2) of the Bankruptcy Act.

3. The Court erred in ruling as a matter of law that only one-fourth of the vacation wages of Appellant's assignors was entitled to priority status as wages under the provisions of Sec. 64a(2) of the Bankruptcy Act.

4. The Court erred in not ruling as a matter of law that vacations with pay provided in the two collective bargaining agreements herein were earned only after all conditions precedent to their earning were complied with by Appellant's assignors.

5. The Court erred in not ruling as a matter of law that all the vacation wages claimed by Appellant's assignors were earned within three months prior to the institution of this bankruptcy proceeding.

6. The Court erred in failing to rule as a matter of law that because the collective bargaining agreements herein did not contain provisions for pro-rata earning of vacations with pay, the referee in bankruptcy was in error when he calculated the earning on a pro-rata basis.

7. The Court erred in ruling as a matter of law that three-fourth's of the vacation pay of Appellant's assignors was entitled to status as a general claim only.

Summary of Argument

- A. VACATION PAY CONSTITUTES WAGES WITHIN THE PROVISIONS OF SEC. 64A(2) OF THE BANKRUPTCY ACT.
- B. PRINCIPLES CONCERNING PRO-RATA EARNING OF VACATIONS ESTABLISHED IN THE CASE OF IN RE PUBLIC LEDGER, INC. DO NOT APPLY TO THE CASE AT BAR.
- C. ALL THE VACATION WAGES OF APPELLANT'S ASSIGNORS WERE ENTITLED TO PRIORITY UNDER THE PROVISIONS OF SEC. 64A(2) OF THE BANKRUPTCY ACT.

ARGUMENT

A. Vacation Pay Constitutes Wages Within the Provisions of Sec. 64a(2) of the Bankruptcy Act.

It is now well established that vacation pay, or pay in lieu of vacation, constitutes "wages" as that term is used in Sec. 64a(2) of the Bankruptcy Act.

In re Public Ledger, Inc. (C.C.A. 3d), 161 F. (2d) 762;

In re Wil-Low Cafeterias, Inc. (C.C.A. 2d), 111 F. (2d) 429;

In re B. H. Gladding Co., 120 Fed. 709.

B. Principles Concerning Pro-Rata Earning of Vacations Established in the Case of *In Re Public Ledger, Inc.* Do Not Apply to the Case at Bar.

In his certificate on review the referee in bankruptcy states that his decision is based on *In re Public Ledger, Inc.*, *supra*. In that case there were collective bargaining agreements containing vacation clauses which specifically called for the pro-rata earning of vacations with pay. The Third Circuit pointed out that the employees under the agreements earned one day's vacation for every twenty-six days worked; as each twenty-six day work period was completed, an employee so working accrued another day's vacation. Since this earning was on a definite pro-rata basis, it was the court's ruling that each employee was entitled to a prior wage claim for the wages he earned during the three months prior to bankruptcy. A District Court in *In re Men's Clothing Authority*

(S.D.N.Y.), 71 Fed. Supp. 469 had previously held the same under similar circumstances.

Herein not only was there no pro-rata vacation provision in either contract, but the Furniture Workers' collective bargaining agreement specifically provided that *there shall be no pro rata vacation*. An employee under one of the agreements involved in the *Public Ledger* case could have quit after fifty-two days' work and been eligible for two days' vacation pay; an employee could have been discharged after two hundred and eight days' work and been eligible for eight days' vacation pay. Under the agreement in the case at bar, an employee who quit or was discharged four, seven or ten months after commencing his year's employment would receive no vacation pay whatsoever; until the year's continuous service was completed, an employee under either agreement earned no vacation whatsoever. For the court below to sustain a ruling wherein pro-rata earning of vacation pay is implied in an agreement where it is specifically excluded is clearly an error. For the court below to hold that an employee earned "something" at the end of nine months, when under the agreement he did not earn "anything" at that time is likewise error.

Vacation pay must be distinguished from ordinary wages. As the minutes, hours, days and weeks of work go by the worker is earning wages, no matter how his pay is computed. At the time his employment ceases he is entitled under the provisions of the California Labor Code to all his wages up to the time of termination. Va-

cation pay is different: the worker is only entitled to it when he has complied with the contractual provisions under which it is allowed. It is conceivable that an employer may contract that vacation pay will be earned coincidental with ordinary wages, but vacation pay ordinarily is based upon completion of some continuous period of service. As was said in the *Wil-Low Cafeterias* case (*supra*):

“A vacation with pay is in effect additional wages. It involves a reasonable arrangement to secure the well being of employees and the continuance of harmonious relations between employer and employee.”

It is only when the employee has fully complied with the conditions precedent to his vacation that he becomes entitled to it; namely, earns it. Typical examples of conditions precedent in vacation contracts are: one day's vacation for every twenty-six days worked; one week's vacation for one year's continuous service; one week's vacation for 1600 straight time hours worked in one fiscal year; one week's vacation for all employees working for at least one year and being on the company payroll as of May 1st of the vacation year; one week's vacation for employees who have been in continuous employment for one year and who have not taken sick leave or other leave in excess of seven days. Prior to complaine in a given situation an employee has earned nothing; after complaine he has earned whatever vacation was promised him.

Appellee urges that for the reasons given and because of the differences in the collective bargaining agreements involved, the ruling of the Third Circuit in the *Public Ledger* case has no application to the case at bar.

C. All the Vacation Wages of Appellant's Assignors Were Entitled to Priority Under the Provisions of Sec. 64a(2) of the Bankruptcy Act.

The courts have held consistently that priority is granted to claims for wages accruing within three months before the date of the commencement of the bankruptcy proceeding, even though the actual services rendered by the employee were performed prior to that time. A leading case on this subject is *In re National Marble & Granite Co.*, 206 Fed. 185. There a salesman worked under an agreement providing for payment of his commission not when he sold the monument but when the monument was delivered and payment made. He sold the monument in March, 1911, and bankruptcy commenced in January, 1912; payment and delivery occurred within three months of bankruptcy. Priority was claimed for the entire commission. The court sustained the claim, stating:

“It is perfectly clear that Brock was not entitled to his compensation until the monument was erected and paid for; all the testimony shows that, although he made the contract for the sale of the monument something like ten months before the bankruptcy proceeding, he was not to receive anything at all for his services in connection with the sale of the monument until the company received the money for it. I cannot escape the conclusion that the commission was not ‘earned’ until the monument was paid for.”

Similar is the case of *In re Magazine Associates, Inc.*, 43 Fed. Supp. 583, in which the claimant was a salesman who procured advertising from Schenley Distillers for publication in Scribner's Magazine. The advertising contract was approved on February 10, 1939, and provided for copy in the February, March, April and May

issues; it could be annulled at any time by the distillers. The employment contract of the salesman provided that he was not to be paid commissions until the 10th of each month following a publication. Bankruptcy commenced on May 26, 1939, more than three months after the sale of the advertising. The court held that the claimant was entitled to priority for his commissions, since the advertiser had the right to cancel and the commission was not earned until after publication or use of the space.

The identical issue was presented herein was determined in the case of *In the Matter of Kinney Aluminum Company, Bankrupt*, No. 44,950-WM, in the same District Court as the instant case. There full priority was claimed for vacation wages under a collective bargaining agreement containing a vacation clause similar to those in the case at bar. The vacation rights accrued after the completion of one year's service and 1600 straight time hours' work. The referee in bankruptcy upheld Appellant's contention that so long as the vacation rights accrued within three months prior to the institution of the bankruptcy proceeding, all of the vacation wages were entitled to priority under Sec. 64a(2) of the Bankruptcy Act. In upholding the referee, District Judge Mathes rendered a Memorandum of Decision wherein he covered the question now before this Court. That portion of Judge Mathes' opinion is herewith set forth:

"Hence these claimants are entitled to receive either one or two weeks' pay in lieu of vacation, depending upon the time each has been 'continuously in the employ of the company.'

"The only question which remains for determination then is whether their claims are entitled to priority of payment pursuant to Sec. 64a(2) of the Bank-

ruptcy Act [11 U.S.C. Sec. 104a(2)]. 'Wages,' within the meaning of Sec. 64a(2), includes vacation pay, or pay in lieu of vacation. [*In re Wil-Low Cafeterias, Inc.*, *supra*, 111 F. (2d) 429; *In re Public Ledger, Inc.*, 161 F. (2d) 762 (C.C.A. 3rd, 1947)]. Accordingly, the narrow issue to be resolved is whether the 'wages . . . have been earned within three months before the date of the commencement of the proceeding . . .' The specific inquiry is whether Congress intended to grant priority to claims for 'wages' accruing within three months prior to bankruptcy, even though part of the services were performed before that time, or to limit priority solely to wage claims based upon services rendered during the three-months' period.

"The purpose of the priority accorded wages is to benefit those not in a position to ascertain the financial status of their employer 'who are dependent upon their wages, and who, having lost their employment by bankruptcy would be in need of such protection.' [*Blessing v. Blanchard*, 223 Fed. 35 (C.C.A. 9th, 1915); *In re Lawsam Electric Co., Inc.*, 300 Fed. 736 (S.D.N.Y., 1924).] There appears no basis in reason or policy to limit the priority to claims for services actually rendered during the three months, as the trustee urges. To achieve fully the protection intended, the priority granted must extend to the wages which accrue to an employee within the period fixed by the Act.

"It is my opinion therefore that Sec. 64a(2) grants a priority to claims for wages accruing 'within three months before the date of the commencement of the proceeding,' even though all the services giving rise to the claims were performed prior to that time. Wages are 'earned,' within the

meaning of Sec. 64a(2), when the right to demand payment accrues. [*In re Magazine Associates, Inc.*, 43 Fed. Supp. 583 (S.D.N.Y., 1942); *In re B. H. Gladding Co.*, 120 Fed. 709 (R.I., 1903); cf. *In re Ko-Ed Tavern, Inc.*, 129 F. (2d) 806 (C.C.A. 3rd, 1942).]

“This conclusion is in no way inconsistent with *In re Public Ledger, Inc.*, *supra*, 161 F. (2d) 762 and *In re Men’s Clothing Code Authority*, 71 Fed. Supp. 469 (S.D.N.Y., 1937) relied upon by the trustee: In those cases, the right of the employees to vacation pay accrued from month to month under the contracts involved; and the courts held that each employee was entitled to a prior claim for the wages which accrued during the three-months’ period preceding bankruptcy.

“Since all conditions precedent to vacation with pay have been satisfied as to the claimants removed from the payroll by bankruptcy on May 5, 1947, their claims accrued on that day—‘the time of termination of service’ * * * ‘during the regularly established vacation period’—and so constitute ‘wages . . . earned within three months before the date of the commencement of the proceeding.’ It follows that these claimants are entitled to have their claims allowed and paid as priority claims pursuant to Sec. 64a(2) of the Bankruptcy Act [11 U.S.C. Sec. 104a(2)].”

Appellant submits that the Fourth Circuit in the case of *Manly v. Hood* (C.C.A. 4th), 37 F. (2d) 212 aptly sets forth the liberal intent of Congress in enacting the priority wage section of the Bankruptcy Act, when it said:

“There can be no question that it was the purpose and intent of Congress, by the provision in question,

to protect the wages of laborers due them by insolvents whose assets had been taken over by the courts under the act. The laborer is generally dependent upon his wages for livelihood and the support of his family, and he has little means of judging of the solvency of his employer. Every consideration of morality, as well as of public policy, demands, therefore, that his wages be preserved to him and be given priority over ordinary commercial claims."

Conclusion.

For the reasons set forth above Appellant respectfully urges that this Court protect the priority rights of the employees of the bankrupt and reverse the orders of the District Judge and the Referee in Bankruptcy.

Respectfully submitted,

PAULINE NIGHTINGALE, and

EDWARD M. BELASCO,

Attorneys for Appellant.

